

RD AN 4156 (4287-B and 4280-B)
March 22, 2006

SUBJECT: Business and Industry Guaranteed and Direct Loan Programs and Section 9006 Renewable Energy Systems and Energy Efficiency Improvements Guaranteed Loans - Loan Classifications

TO: State Directors, Rural Development

ATTN: Business Program Directors

PURPOSE AND INTENDED OUTCOME:

This Administrative Notice is designed to emphasize the requirement and importance of appropriate and timely classification of Business and Industry (B&I) and Section 9006 Renewable Energy Systems and Energy Efficiency Improvements (Section 9006) Guaranteed Loans.

COMPARISON WITH PREVIOUS AN:

This replaces RD AN 4129, dated December 13, 2005.

IMPLEMENTATION RESPONSIBILITIES:

B&I and Section 9006 guaranteed loans are required to be properly classified. As we face challenges with human resource capitalization, it is important that we focus attention on the loan identified as the highest risk. Managing the portfolio effectively dictates the need for identifying those areas of high risk. Loan classification is a tool to accomplish effective portfolio management. Loan classification will be used by the National Office and State Offices to assist in risk assessment. By properly classifying B&I and Section 9006 guaranteed loans, the Agency can better assess potential risks within the portfolios and assist with the focus resources accordingly.

Within 90 days after the Agency issues the Loan Note Guarantee, the Lender must notify the Agency of the loan's classification or rating under its regulatory standards. The Lender must also notify the Agency when there is a change in the original loan

EXPIRATION DATE:
March 31, 2007

FILING INSTRUCTIONS:
Preceding Instructions 4287-B and 4280-B

classification. When the Agency receives the loan classification from the Lender, the Agency is required to classify the B&I or Section 9006 loan within 30 days of receiving the Lender's classification in the Guaranteed Loan System (GLS). In the event the Lender uses a different classification system than GLS, the Agency must convert the Lender's classification to one that closely corresponds with the internal GLS. The integrity of the data in GLS is vitally important, and every effort should be made to maintain GLS in a current status. The loan classification code is maintained on the Business Programs Loan/Grant Detail screen. The screen can be found by going to the Request List, inputting the borrower's ID, and on the Action dropdown box, highlight "Maintain Loan/Grant Detail" and click on the type of assistance code. The loan classification is a dropdown box with the codes as described below. If a borrower has a direct loan, an 8N transaction must be completed in ADPS and will interface with GLS with the corresponding code listed below. For further instructions, please review the GLS User Guide Section 5.

The B&I and Section 9006 loan classifications should be discussed during the annual Lender visit and the GLS updated within 30 days thereafter. There are six loan classifications within GLS and are discussed below:

10 – Current Non-problem Classification

Those loans that are current and are in compliance with all loan conditions of B&I or Section 9006 regulations but do not meet all of the criteria for Seasoned Loan classification.

20 – Seasoned Loan Classification

A loan which (1) has a remaining principal guaranteed loan balance of two-thirds or less of the original aggregate of all existing B&I or Section 9006 guaranteed loans made to that business; (2) is in compliance with all loan conditions and B&I or Section 9006 regulations; and (3) has been current on the B&I or Section 9006 guaranteed loan(s) payments for 24 consecutive months, and is secured by collateral which is determined to be adequate to insure there will be no loss on the B&I or Section 9006 guaranteed loan.

30 – Special Mention Classification

Those loans which do not presently expose the Lender and Agency to a sufficient degree of risk to warrant a substandard classification but do possess credit deficiencies deserving the Lender's close attention, and failure to correct these deficiencies could result in a greater loss. This classification would include failure to obtain proper documentation or any other deviations from prudent lending practices, an inadequate loan agreement, i.e. (business is consistently out of compliance with loan covenants or agreement does not

meet regulatory guidelines), adverse trends in the borrower's operation or an imbalanced position in the balance sheet, i.e. liabilities exceed assets, which has not reached a point that jeopardizes the repayment of the loan should be assigned to this designation, loans in which actual, not potential, weaknesses are evident and significant should be considered for this classification.

40 – Substandard Classification

Those loans which are inadequately protected by a current sound worth and paying capacity of the obligor or to the collateral, pledged, if any. Loans in this category must have a well-defined weakness or weaknesses that jeopardize the payment in full of the debt. If the deficiencies are not corrected, there is a distinct possibility that the Lender and Rural Development will sustain some loss.

50 – Doubtful Classification

Those loans which have all the weaknesses inherent in those classified substandard, with the added characteristics that the weaknesses make collection or liquidation in full, based on currently known facts, conditions, and values (highly questionable and improbable).

60 – Loss Classification

Those B&I and Section 9006 loans which are considered uncollectible and of such little value that their continuance as bankable loans is not warranted. Even though partial recovery may be affected in the future, it is not practical or desirable to defer writing off these basically worthless loans.

Please make every effort to get loan classifications up-to-date in working with the Lenders. It is imperative that GLS is updated accordingly. Your efforts will assist this office in fiscal year 2007 planning efforts.

If you have any questions or concerns, please contact the B&I Loan Servicing Branch at (202) 690-4103 or the Specialty Lenders Division Servicing Branch at (202) 690-4106.

(Signed by Jackie J. Gleason)

JACKIE J. GLEASON
Acting Administrator
Business and Cooperative Programs